Supreme Court, U.S.
FILED

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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

FLOYD E. RILEY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

Petition for Writ of Certiorari to the
United States Court of Appeals for the Eighth Circuit

PETITION FOR WRIT OF CERTIORARI

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29 pp.

QUESTION PRESENTED

Whether an act in violation of 11 U.S.C. § 362 and all actions subsequent thereto are void or voidable.

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
STATEMENT OF JURISDICTION	1
STATUTORY PROVISION INVOLVED	1
STATEMENT OF THE CASE	2
REASONS FOR GRANTING THE WRIT	4
THE EIGHTH CIRCUIT'S HOLDING CONFLICTS WITH DECISIONS OF OTHER UNITED STATES CIRCUIT COURTS OF APPEAL AND IS CONTRARY TO AN EXISTING DECISION OF THE UNITED STATES SUPREME COURT AND THE LANGUAGE AND INTENT OF THE UNITED STATES BANKRUPTCY CODE.	4
I. The Eighth Circuit's Decision is Inconsistent with a Majority of Circuit Courts Which Have Held that Violations of the Automatic Stay are Void *Ab Initio*.	4
II. The Eighth Circuit's Decision is Also Inconsistent with the Minority of Circuit Courts Which Have Held that Violations of the Automatic Stay Are Voidable.	7
CONCLUSION	10

TABLE OF AUTHORITIES

Page(s)

Cases:

Bronson v. United States, 46 F.3d 1573 (Fed.Cir. 1995) 7

Constitution Bank v. Tubbs, 68 F.3d 685 (3d Cir. 1995) 4

Easley v. Pettibone Michigan Corp., 990 F.2d 905 (6th Cir. 1993) 7-8

Franklin v. Office of Thrift Supervision, 31 F.3d 1020 (10th Cir. 1994) 4

Kalb v. Feurstein, 308 U.S. 433, 60 S.Ct. 343, 84 L.Ed. 370 (1940) 4

Matthews v. Rosene, 739 F.2d 249 (7th Cir. 1984) 4

National Labor Relations Board v. Edward Cooper Painting, Inc., 804 F.2d 934 (6th Cir. 1986) 7

Pennsylvania Public Welfare Dept. v. Davenport, 495 U.S. 552, 110 S.Ct. 2126, 109 L.Ed.2d 558 (1990) 5

Picco v. Global Marine Drilling Co., 900 F.2d 846 (5th Cir. 1990) 7

In re Albany Partners, 749 F.2d 670 (11th Cir. 1984) 4

In re Calder, 907 F.2d 953 (10th Cir. 1990) 8

In re Schwartz, 954 F.2d 569 (9th Cir. 1992) 4-6, 8

In re Smith, 876 F.2d 524 (6th Cir. 1989) 7

In re Smith Corset Shops, 696 F.2d 971 (1st Cir. 1982) 8

In re Soares, 107 F.3d 969 (1st Cir. 1997) 4,6

Rexnord Holdings, Inc. v. Bidermann, 21 F.3d 522 (2d Cir. 1994) 4

Sikes v. Global Marine, Inc., 881 F.2d 176 (5th Cir. 1989) 8-9

Statutes:

11 U.S.C. § 101(50) 8

11 U.S.C. § 105 8

11 U.S.C. § 362 ..... *passim*

11 U.S.C. § 549 8-9

11 U.S.C. 701 *et seq.* 2

26 U.S.C. § 6672 ..... *passim*

28 U.S.C. § 1331 2

28 U.S.C. § 1346(a)(1) 2

Other:

H.R.Rep. 595, 95th Cong., 1st Sess. 340 (1978), *reprinted in* 1978 U.S.Code Cong. & Admin. News 5963 5

S.Rep. 95-989, 95th Cong., 2d Session 54 (1978), *reprinted in* 1978 U.S.Code Cong. & Admin. News 5787 5

2 *Collier on Bankruptcy* § 362.07 7

PETITION FOR WRIT OF CERTIORARI

Petitioner Floyd E. Riley respectfully requests that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Eighth Circuit entered in this action on July 7, 1997 reversing the final judgment of the United States District Court for the Eastern District of Missouri.

OPINIONS BELOW

On October 25, 1995, the United States District Court for the Eastern District of Missouri held that the notice of proposed assessment issued by the Internal Revenue Service during Petitioner's bankruptcy case violated the automatic stay, 11 U.S.C. § 362, and, thus, the subsequent assessment was void. The decision is reported at 192 B.R. 727 (E.D.Mo. 1995). The United States Court of Appeals for the Eighth Circuit reversed this decision and remanded for further proceedings. This decision is reported at 118 F.3d 1220 (8th Cir. 1997). Without discussion, the Eighth Circuit denied Petitioner's suggestion for rehearing *en banc*. The decisions are reprinted in Appendices A-1 and A-7, *infra*.

STATEMENT OF JURISDICTION

The judgment of the Court of Appeals for the Eighth Circuit was entered on July 7, 1997. Jurisdiction is conferred on this Court by 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

11 U.S.C. § 362

STATEMENT OF THE CASE

In 1991, Ferco Fabricators, Inc. ("Ferco") was bankrupt and filed for relief under Chapter 7 of the United States Bankruptcy Code, 11 U.S.C. 701 *et seq.*[1] Although Respondent Internal Revenue Service ("IRS") held a priority position in the bankruptcy case, the IRS failed to take any action to liquidate Ferco's assets that would have satisfied the $683,675.24 owed for withholding taxes.

Shortly thereafter, Petitioner Floyd E. Riley ("Riley") also filed Chapter 7. While his case was still pending, the IRS issued Riley a Notice of Proposed Assessment (the "Notice") pursuant to 26 U.S.C. § 6672 demanding a 100 percent penalty for *Ferco's* failure to pay these same withholding taxes.

The Notice allowed Riley 30 days to pay $683,675.24 or appeal the Notice to the IRS. Still bankrupt, Riley appealed. Taking longer than one year and even beyond the end of Riley's bankruptcy case, the IRS eventually denied Riley's appeal and assessed the proposed amount. Pursuant to statute, Riley paid the IRS $2,000.00 and commenced a refund and abatement action in the United States District Court for the Eastern District of Missouri; jurisdiction was conferred under 28 U.S.C. §§ 1331 and 1346(a)(1). The IRS counterclaimed for the remainder of the penalty.

The district court granted Riley's motion for summary judgment holding that as a matter of law the Notice was issued during Riley's bankruptcy case in violation of 11 U.S.C. § 362 (the "Automatic Stay") and was void. A-5. The district court further held that even if the IRS was not required to issue the Notice prior

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[1] All references to the United States Bankruptcy Code (the "Bankruptcy Code") are to 11 U.S.C. *et seq.*, 1988 edition, unless specifically noted. The 1994 Amendments to the Bankruptcy Code are not retroactive with respect to the provisions discussed herein.

to assessment, it was undisputed that the IRS, in fact, did so which forced Riley to defend himself in an administrative appeal that resulted in assessment. A-5. Therefore, the assessment was void *ab initio*. The district court decision is reported at *Riley v. United States*, 192 B.R. 727 (E.D.Mo. 1995).

The IRS appealed to the United States Court of Appeals for the Eighth Circuit. The Eighth Circuit reversed the district court holding that although the IRS knowingly violated the Automatic Stay by issuing the Notice, the resulting assessment occurred after Riley was discharged from bankruptcy and, thus, was not void and was an otherwise irrelevant defense to a refund action. A-9, A-10. This decision is reported at 118 F.3d 1220 (8th Cir. 1997).

Riley now timely files this Petition for Writ of Certiorari with this Court.

REASONS FOR GRANTING THE WRIT

THE EIGHTH CIRCUIT'S HOLDING CONFLICTS WITH DECISIONS OF OTHER UNITED STATES CIRCUIT COURTS OF APPEAL AND IS CONTRARY TO AN EXISTING DECISION OF THE UNITED STATES SUPREME COURT AND THE LANGUAGE AND INTENT OF THE UNITED STATES BANKRUPTCY CODE.

I. The Eighth Circuit's Decision is Inconsistent with a Majority of Circuit Courts Which Have Held that Violations of the Automatic Stay are Void *Ab Initio*.

Although the IRS is one of the largest and most sophisticated creditors, the Eighth Circuit in this case has dismantled one of the few protections available to keep this governmental Goliath and other creditors at bay. There is no dispute that the IRS violated the Automatic Stay when it issued Riley the Notice. However, the Eighth Circuit held that whether this act and those subsequent thereto are void or voidable is a theoretical distinction and otherwise irrelevant to a refund action. A-9, A-10. This decision cannot be reconciled with the holdings of a majority of the circuit courts declaring such acts void *ab initio*. *In re Soares*, 107 F.3d 969 (1st Cir. 1997); *Constitution Bank v. Tubbs*, 68 F.3d 685 (3d Cir. 1995); *Franklin v. Office of Thrift Supervision*, 31 F.3d 1020 (10th Cir. 1994); *Rexnord Holdings, Inc. v. Bidermann*, 21 F.3d 522 (2d Cir. 1994); *In re Schwartz*, 954 F.2d 569, 572 (9th Cir. 1992); *In re Albany Partners*, 749 F.2d 670, 675 (11th Cir. 1984); *Matthews v. Rosene*, 739 F.2d 249, 251 (7th Cir. 1984). Even this Court has held (under a predecessor to the Automatic Stay) that creditors must not benefit from their unlawful acts and, thus, they are void and subject to collateral attack. *E.g., Kalb v. Feurstein*, 308 U.S. 433, 443, 60 S.Ct. 343, 348, 84 L.Ed. 370 (1940)(sheriff's sale during bankruptcy void and all subsequent actions taken also void).

Concluding that acts in violation of the Automatic Stay are void, a majority of circuit courts have each recognized and emphasized the sweeping language, the self-executing nature of the Automatic Stay and the essential function it serves in the administration of the bankruptcy estate. The Automatic Stay does not extinguish or discharge any debts. *Pennsylvania Public Welfare Dept. v. Davenport*, 495 U.S. 552, 560 n.3, 110 S.Ct. 2126, 109 L.Ed.2d 558 (1990). It merely grants the debtor a brief respite from creditors' claims and attempts to preserve the status quo so that assets may be collected and reorganized or liquidated in an orderly manner. H.R.Rep. 595, 95th Cong., 1st Sess. 340 (1978), *reprinted in* 1978 U.S.Code Cong. & Admin. News 5963, 6296-97. This benefits not only debtors by providing them a breathing spell but also creditors by allowing the courts and trustees time and ability to gather the property of the estate for their collective benefit. *See* S.Rep. 95-989, 95th Cong., 2d Session 54 (1978), *reprinted in* 1978 U.S.Code Cong. & Admin.News, pp. 5787, 5849. This function is defeated if a single creditor is allowed to violate the Automatic Stay pillaging a debtor's assets in order to collect a debt or forcing the debtor to spend time and resources to defend himself as Riley was forced to do in this case.

It is this attempt to circumvent and undermine the bankruptcy process itself that has drawn the greatest fire from the circuit courts. As thoroughly explained by the Ninth Circuit in *In re Schwartz*, the debtor is trying to regain his financial footing and should not face the additional hardship of fending off creditors who violate the Automatic Stay. *Schwartz*, 954 F.2d at 571-72. The debtor in *Schwartz* challenged an assessment by the IRS for withholding tax penalties asserting that it violated the Automatic Stay and was void *ab initio*. *Id.* at 575. The Ninth Circuit agreed warning that if the unlawful acts are not unmistakably void, creditors will be encouraged to violate the Automatic Stay and risk a potential challenge by a weakened debtor.

> If violations of the stay are merely voidable, debtors must spend a considerable amount of time and money policing and litigating creditor actions. If violations are void, however, debtors are afforded better protection and can focus their attention on reorganization.
>
> * * *
>
> Nothing in the Code or legislative history suggests that Congress intended to burden a bankruptcy debtor with an obligation to fight off unlawful claims. The position championed by the IRS in this case [that a § 6672 assessment in bankruptcy is not void] would impose severe hardships on debtors trying to regain their financial footing.

Id. at 571-72.

The Eighth Circuit circumvented the void/voidable dilemma declaring that the Automatic Stay, which Riley asserted as a complete defense to the IRS's claims, was irrelevant to a refund action and merely a theoretical distinction that it refused to address. A-9, A-10. It rejected the district court's adoption of *Schwartz* declaring the IRS's acts void and, in effect, shifted the burden far beyond that of any other circuit court creating a presumption of validity in favor of the creditor. Under this unprecedented interpretation, the efficacy of the Automatic Stay in the Eighth Circuit is now in doubt.

The purpose of the Automatic Stay was not to allow creditors to test the waters to determine whether an act violates the stay. The idea was to create a menacing figure, actually feared by creditors, that stopped creditors at the water's edge. "[C]ourts must display a certain rigor in reacting to violations of the automatic stay." *Soares*, 107 F.3d at 975-976. By voiding such acts and attaching fees and even punitive damages, the Automatic Stay puts creditors on notice that if they violate it, they risk losing even more than they sought. This was the intent of

Congress and the foundation of the majority view, a view that cannot be reconciled with the approach taken by the Eighth Circuit in this cause.

II. The Eighth Circuit's Decision is Also Inconsistent with the Minority of Circuit Courts Which Have Held that Violations of the Automatic Stay Are Voidable.

The approach of the Eighth Circuit is far from consonant with even the minority of circuit courts holding that actions in violation of the Automatic Stay are voidable. *Bronson v. United States*, 46 F.3d 1573 (Fed.Cir. 1995); *Easley v. Pettibone Michigan Corp.*, 990 F.2d 905, 909-11 (6th Cir. 1993); *Picco v. Global Marine Drilling Co.*, 900 F.2d 846 (5th Cir. 1990).[2] Instead of looking to the language and purpose of the Automatic Stay, the minority view has contrasted it with other provisions of § 362 and the Bankruptcy Code finding several sections inoperable or rendered moot if actions violating the Automatic Stay are void.

The Sixth Circuit in *Easley v. Pettibone Michigan Corp.* looked first to the Bankruptcy Court's power to "annul" the Automatic Stay pursuant to § 362(d). "This power to annul 'permits the order to operate retroactively, thus validating actions taken by a party at a time when he was unaware of the stay.'" *Easley*, 990 F.2d at 910, *quoting* 2 *Collier on Bankruptcy* § 362.07. The circuit court thus concluded that in order to harmonize the language of the Automatic Stay with the power to annul, actions in violation of the Automatic Stay must be characterized as "invalid and voidable, since void actions are incapable of later cure or validation." *Easley*, 990 F.2d at 910. The Sixth Circuit similarly noted that where several circuits (including those in the majority) have used their equitable

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[2] The position of the Sixth Circuit is unclear with two panels holding violations void and another holding them voidable. *Compare Easley*, *supra*; *In re Smith*, 876 F.2d 524 (6th Cir. 1989)(void); *National Labor Relations Board v. Edward Cooper Painting, Inc.*, 804 F.2d 934 (6th Cir. 1986)(void).

powers (presumably under 11 U.S.C. § 105) to forestall the operation of the Automatic Stay, "these circuits are really viewing actions taken in violation of the stay as voidable." 990 F.2d at 910, *citing In re Calder*, 907 F.2d 953 (10th Cir. 1990); *Matthews*, 739 F.2d 249; *In re Smith Corset Shops*, 696 F.2d 971 (1st Cir. 1982).

The Sixth Circuit further rejected the majority view that the power to annul under § 362(d) operates as a narrow exception to the broad general rule (in subsection (a)) that acts in violation of the stay are void. *Easley*, 990 F.2d at 910; *see Schwartz*, 954 F.2d at 573 (absent affirmative relief from the court, violations of the Automatic Stay are void). The Sixth Circuit explained that such characterization should manifest at the time of the violation and not later if and when a creditor obtains relief under § 362(d). This merely creates an unnecessary legal fiction. *Id.* Instead, because the power to annul the Automatic Stay under § 362(d) allows the court to validate a previously invalid act, the Sixth Circuit concluded that, by definition, the act must be voidable. 990 F.2d at 919-910.

Finally, circuits in the minority raise a more troubling conflict between a void act under the Automatic Stay and the operation of 11 U.S.C. § 549. *See, e.g., Sikes v. Global Marine, Inc.*, 881 F.2d 176, 179 (5th Cir. 1989). Under § 549, the bankruptcy trustee may avoid certain authorized transfers[3] and all unauthorized transfers of estate property regardless of the Automatic Stay. *Id.* Because the definition of transfer is so broad, the minority view posits that the Automatic Stay and § 549 can apply to the same transactions. *Id.* However, § 549 implies that such transfers are valid unless challenged by the trustee. Therefore, violations under the Automatic Stay cannot be declared void for

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[3] "Transfer" is "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property. . . ." 11 U.S.C. § 101(50).

§ 549 would effectively be rendered moot. *Id.* Unable to reconcile these competing sections of the Bankruptcy Code, the minority of circuit courts have concluded that because violations of the Automatic Stay can be annulled or avoided, such acts must be characterized as voidable.

In each of the aforementioned examples, the decision of the circuit court hinged upon a creditor's ability to seek retroactive relief through sections other than the Automatic Stay. The Eighth Circuit, however, refused to address this issue and, in effect, annulled the Automatic Stay and ratified the IRS's actions without any statutory authority creating further confusion among the courts of this and other circuits.

CONCLUSION

The Automatic Stay is the cornerstone of the Bankruptcy Code. Without it, creditors, like vultures, will devour what assets exist in a frenzy leaving bankruptcy courts with nothing to distribute but mere crumbs and little real power to stop the violators. Priorities will mean nothing. Instead, the largest, most sophisticated creditors like the IRS will hover over debtors and take all within their grasp. By overlooking this split of opinion on such an important issue, the Eighth Circuit inadvertently created yet a third view unprecedented in bankruptcy law jurisprudence. By refusing to punish the IRS for its flagrant violation of the Automatic Stay, the Eighth Circuit opened the gate for other creditors to trample upon the rights of debtors leaving the efficacy of the Code uncertain. Therefore, Riley respectfully requests this Supreme Court to grant his Petition for Writ of Certiorari in order to resolve this important question of federal law.

Respectfully submitted,

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APPENDIX A

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

No. 2:94CV00124 GFG

FLOYD E. RILEY,
Plaintiff,

vs.

UNITED STATES OF AMERICA,
Defendant.

MEMORANDUM

This matter is before the Court on plaintiff's Motion for Summary Judgment. On November 2, 1994 plaintiff brought suit against the United States to recover $2,000, plus interest, representing a penalty paid to the IRS pursuant to 26 U.S.C. § 6672. Thereafter, the United States filed a counterclaim against plaintiff for the unpaid balance of such penalty in the amount of over $650,000. Plaintiff has filed a motion for summary judgment. Defendant opposes that motion.

Rule 56(c) of the Federal Rules of Civil Procedure provides that summary judgment shall be entered "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." In ruling on a motion for summary judgment, the court is required to view the facts in the light most favorable to the non-moving party and must give that party the benefit of all reasonable inferences to be drawn from the underlying facts. *AgriStor Leasing v. Farrow*, 826 F.2d 732, 734 (8th Cir. 1987). The moving party bears the burden of showing both the absence of a genuine issue of material fact and

his entitlement to judgment as a matter of law. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986); *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586-87 (1986); Fed. R. Civ. P. 56(c).

Once the moving party has met his burden, the non-moving party may not rest on the allegations of his pleadings but must set forth specific facts, by affidavit or other evidence, showing that a genuine issue of material fact exists. Fed. R. Civ. P. 56(e). *Anderson*, 477 U.S. at 257; *City of Mt. Pleasant v. Associated Elec. Coop., Inc.*, 838 F.2d 268, 273-74 (8th Cir. 1988). Rule 56(c) "mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986).

The Internal Revenue Service ("IRS") may impose a 100% penalty against persons responsible for the collection of employee withholding taxes who willfully fail to pay over those taxes. 26 U.S.C. § 6672. The parties agree that the IRS assessed such a penalty against plaintiff in the amount of $683,675.24. The assessment was for employee withholdings made in first, second, and third quarters of 1990 allegedly not paid to the IRS by a company known as FERCO Fabricators, Inc. ("FERCO").

The following facts are not disputed. On September 17, 1991 after the taxes at issue were due, plaintiff filed for bankruptcy protection under Chapter 7 of the Bankruptcy Code. (Pl. Exh. 1.) On May 18, 1992 the IRS sent plaintiff a Notice of Proposed Assessment of the § 6672 penalty; the notice warned plaintiff that the threatened penalty would be processed if he did not protest it within 30 days. (Pl. Exh. 3.) In a letter dated June 8, 1992 plaintiff, through his attorneys, advised the IRS that the proposed assessment violated the automatic stay provisions of

11 U.S.C. § 362(a). (Pl. Exh. 4.) The IRS disagreed with plaintiff's position and on June 16, 1992 plaintiff appealed the IRS's assessment by mailing a protest letter. (Pl. Exh. 2.) On June 30, 1992 the Bankruptcy Court entered its discharge order. (Pl. Exh. 5.) Mr. Riley's appeal of the proposed assessment was eventually denied and the purported assessment was made the following year. Later, after paying $2,000 of the penalty, plaintiff initiated this action.

Under the version of § 362 of the Bankruptcy Code applicable to this case,[1] the filing of a bankruptcy petition operates as a stay and blocks "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title." 11 U.S.C. § 362(a)(6). However, the filing of a petition does not operate to stay "the issuance to the debtor by a government unit of a notice of tax deficiency." 11 U.S.C. § 362(b)(9).

There is a split among the circuits regarding whether violations of the automatic stay are void or voidable. The Fifth Circuit has held that the violations of the automatic stay are voidable. *Picco v. Global Marine Drilling Co.*, 900 F.2d 846 (5th Cir. 1990); *Sikes v. Global Marine, Inc.*, 881 F.2d 176 (5th Cir. 1989). The First, Second, Third, Sixth, Ninth, Tenth, and Eleventh Circuits have all held that violations are void *ab initio*. *Schwartz v. United States*, 954 F.2d 569 (9th Cir. 1992); *Ellis v. Consolidated Diesel Elec. Corp.*, 894 F.2d 371 (10th Cir. 1990); *Smith v. First American Bank*, 876 F.2d 524 (6th Cir. 1989); *In re Ward*, 837 F.2d 124 (3d Cir. 1988); *48th Street Steakhouse, Inc. v. Rockefeller Group, Inc.*, 835 F.2d 427 (2d Cir. 1987), *cert. denied*, 485 U.S. 1035 (1988); *Borg-Warner Acceptance Corp. v. Hall*, 685 F.2d 1306 (11th Cir. 1982); *In re Smith Corset*

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[1] The Bankruptcy Code was amended in 1994, but the amendments are not retroactive. Bankruptcy Code Amendments of 1994, Pub. L. No. 103-394, § 702(b), 108 Stat. 4107 (codified in scattered sections of 11 U.S.C.).

Shops, Inc., 696 F.2d 971 (1st Cir. 1982). The Eighth Circuit has not yet addressed this issue. This Court finds persuasive and adopts the reasoning herein of the majority of courts addressing this issue. Therefore, any violation of the automatic stay will be deemed void *ab initio.*

In this case, the plain language of § 362(b)(9) protects only notices of tax "deficiencies," not "penalties" and forecloses the government's argument that a § 6672 "penalty" is similar enough to a "deficiency" to be exempted from the automatic stay. The government also contends that the Notice of Proposed Assessment in this case did not constitute an assessment of or an effort to collect the liability. However, the government describes the effect of the notice sent in this case as follows:

> [I]n the event a Trust Fund Recovery Penalty is asserted [under § 6672], the taxpayer will not be sent a notice of deficiency. Rather, the IRS sends a Notice of Proposed Assessment to the taxpayer allowing him either to agree to the assessment by signing the Form 2751 or providing a thirty-day period within which to appeal the proposed assessment by filing a protest with the Secretary. If the taxpayer agrees to the assessment, fails to respond to the notice, or fails to present sufficient facts in his protest to support non-assertion of penalty, the IRS will assess the taxpayer a penalty.

(Def. Resp. to Pl. Mot. for Summ. J. at 6.) The effect of the Notice was to force plaintiff to take steps to prevent the assessment and had plaintiff not taken such steps the IRS would have assessed the penalty while the automatic stay was still in effect. The Notice described above clearly falls within the range of acts prohibited by § 362(a) as they are designed to initiate assessment against the debtor of a claim that arose prior to the filing of his bankruptcy petition. Cf. *Schwartz v. United States*, 954 F.2d 569 (9th Cir. 1992); *Spears v. United States*, 143 B.R. 950 (N.D. Okla. 1992); *Olson v. United States*, 133 B.R. 1016 (D. Neb.

1991). Therefore, the Notice of Proposed Assessment at issue violated the automatic stay such that it is void *ab initio.*

The government further argues that the Notice was not a mandatory procedure in its efforts at assessing the penalty, and that therefore the fact that the Notice was sent while the automatic stay was in effect does not effect the validity of the assessment made after discharge. While the IRS may not have been required to follow those procedures which resulted in the assessment, it nevertheless did and those procedures initiated with the Notice forced plaintiff while protected by a stay to participate in procedures which led to the assessment in this case. Accordingly, the Court will grant plaintiff's Motion for Summary Judgment.

Dated this 25th day of October, 1995.

/s/ George F. Gunn, Jr.
GEORGE F. GUNN, JR.
UNITED STATES
DISTRICT JUDGE

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

No. 2:94CV00124 GFG

FLOYD E. RILEY,
Plaintiff,

vs.

UNITED STATES OF AMERICA,
Defendant.

JUDGMENT

Pursuant to the memorandum filed herein on this date,

IT IS HEREBY ORDERED that plaintiff's Motion for Summary Judgment is granted.

IT IS FURTHER ORDERED that defendant's Motion for Summary Judgment is denied.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that judgment is entered in favor of plaintiff and against defendant on plaintiff's complaint in the amount of $2,000 plus interest.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that judgment is entered in favor of plaintiff and against defendant on defendant's counterclaim.

IT IS FURTHER ORDERED that all other pending motions are denied as moot.

Dated this 25th day of October, 1995.

/s/ George F. Gunn, Jr.
GEORGE F. GUNN, JR.
UNITED STATES
DISTRICT JUDGE

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

Nos. 96-1021/96-1302

Floyd E. Riley,
Appellee/Cross-Appellant,

v.

United States of America,
Appellant/Cross-Appellee.

Appeal and Cross-Appeal from the United States District Court for the Eastern District of Missouri.

Submitted: April 14, 1997
Filed: July 7, 1997

Before McMILLIAN, Circuit Judge, HENLEY, Senior Circuit Judge, and BEAM, Circuit Judge.

BEAM, Circuit Judge.

The United States appeals the district court's summary judgment order concluding that Floyd E. Riley is entitled to a $2,000 tax refund. Riley cross-appeals the court's denial of his motion for attorney fees. We reverse the court's summary judgment order and remand for further proceedings.

I. BACKGROUND

Through 1990, Floyd E. Riley was associated, in various capacities, with Ferco Fabricators, Inc., a company in Moberly, Missouri. During this time Riley was majority shareholder and at one point served as chairman of the board of directors. The government alleges that in 1990, while Riley was still involved with Ferco, the company failed to remit to the government more

than $680,000 it had withheld from employees for social security and income taxes.

Riley filed for Chapter 7 bankruptcy in September of 1991, and received his discharge in June of 1992. During this time, the Bankruptcy Code's automatic stay was in effect, entitling Riley to protection from all actions to recover claims against him that arose before he filed his bankruptcy petition. *See* 11 U.S.C. § 362(a)(6).

On May 18, 1992, during the period of the automatic stay, the Internal Revenue Service issued to Riley a notice of proposed assessment of a penalty for Ferco's unpaid taxes, pursuant to I.R.C. § 6672. The notice informed Riley that he could either agree to pay the proposed assessment or could file an appeal with the agency within thirty days. Riley protested the proposed assessment, claiming that it violated the automatic stay and that, in any event, he was not responsible. In August of 1993, more than a year after the stay expired, the IRS issued the assessment. Riley paid $2,000, representing a portion of the assessment, and made a claim for a refund. After the IRS denied his claim, Riley brought this refund action in the district court.

On Riley's motion for summary judgment, the district court found that the notice of proposed assessment violated the automatic stay. The district court concluded that this rendered the assessment void and granted Riley's request for a refund. *Riley v. United States*, 192 B.R. 727, 730 (E.D. Mo. 1995). In a later order, the court denied Riley's request for attorney fees and costs, concluding that the IRS's position, though erroneous in the court's view, was substantially justified. The government appeals the court's grant of summary judgment, and Riley appeals the denial of his motion for fees.

II. DISCUSSION

When a corporation fails to pay withheld employee "trust fund" taxes, the IRS may impose a penalty equal to one hundred

percent of the deficiency on any individual who is a "responsible person" and who willfully failed to pay the taxes. I.R.C. § 6672. *Olsen v. United States*, 952 F.2d 236, 239 (8th Cir. 1991). A section 6672 assessment is presumed correct, and it is the individual's burden to show, in a refund action, that he or she was not a responsible person or did not willfully fail to pay over the taxes. *Id.*

Under the version of the Bankruptcy Code applicable to this case, a notice of deficiency from the IRS to a taxpayer is specifically exempted from the automatic stay provision. *See* 11 U.S.C. § 362(b)(9) (1988). The district court rejected the agency's argument that a notice of proposed assessment under section 6672 is the same as a "notice of deficiency" for purposes of the stay, and therefore concluded that the IRS's actions were not exempted from the stay requirements. The agency apparently concedes this issue on appeal. Indeed, assuming that a notice of proposed assessment was not exempted from the stay requirements of the applicable version of the Bankruptcy Code, it is apparent that the agency's proposed assessment to Riley violated the stay. The notice forced Riley to either submit to the assessment, pursue appeals within the agency, or (as Riley did) make a partial payment and then bring a refund action. The proposed assessment thus intruded on the period of repose that the automatic stay provides the bankruptcy petitioner.

The actual assessment, however, was issued long after the automatic stay expired. Riley argues, and the district court concluded, that the agency's issuance of the *notice* of proposed assessment during the stay renders the subsequent assessment "void ab initio."[1] Riley suggests two ways that the improper

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[1] The district court held that the stay violation rendered the assessment void ab initio, rather than merely "voidable." *Riley*, 192 B.R. at 729. We find this theoretical question beside the point in this case, and so decline to address it.

issuance of the notice might render the later assessment void. We find neither theory persuasive.

First, the assessment might be invalid if the improperly issued notice means that the IRS failed to follow required procedures, and so failed to perfect its claim. The problem for Riley is that at the time of the events in question, the Internal Revenue Code did not require the agency to issue any notice before assessing a penalty under section 6672. Not until 1996 did Congress amend section 6672 to require the agency to issue a preliminary notice to the taxpayer before imposing an assessment. *See* Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 901(a), 110 Stat. 1452, 1465 (1996) (codifying notice requirement at 26 U.S.C. § 6672 (b)). Riley argues that Revenue Procedure 84-78, 1984-2 C.B. 754 (1984), imposed such a requirement. Revenue Procedures that involve distinctly procedural matters not otherwise controlled by statute, however, are not binding on the agency. *See, e.g., Estate of Jones v. Commissioner*, 795 F.2d 566, 571-72 (6th Cir. 1986). Neither the Bankruptcy Code nor the Internal Revenue Code requires that we render "void ab initio" an assessment for $680,000 in unpaid taxes because that assessment was issued after a "void" notice that the agency was under no obligation to issue in the first place.

Second, Riley suggests, it is proper to void the assessment because this would be a proper remedy for the agency's earlier violation of the stay. Any damages Riley incurred from responding to the agency's proposed assessment, however, were a matter for the bankruptcy court. Whatever remedy Riley might be entitled to for the IRS's stay violation is irrelevant to his burden in bringing this refund action: to show that he was not a responsible person or that he did not act willfully in failing to pay Ferco's trust fund taxes.

Because we hold that the IRS should have prevailed below on Riley's motion for summary judgment, we affirm on that basis the district court's denial of Riley's motion for attorney fees.

III. CONCLUSION

The district court's grant of summary judgment to Riley is reversed, and the denial of Riley's motion for attorney fees is affirmed. The case is remanded for further proceedings not inconsistent with this opinion.

A true copy.

ATTEST:

CLERK, U.S. COURT OF APPEALS,
EIGHTH CIRCUIT

APPENDIX C

11 U.S.C. § 362 Automatic Stay (1988 ed.)

(a) Except as provided in subsection (b) of this section, a petition filed under [the Bankruptcy Code] . . . operates as a stay, applicable to all entities, of —

(1) The commencement . . . of . . . [an] administrative, or other action or proceeding against a debtor that . . . could have been commenced before the commencement of the case under this title, or to recover a claim against a debtor that arose before the commencement of the case under this title; . . .

(6) Any act to collect, assess, or recover a claim against a debtor that arose before the commencement of the case under this title. . . .

* * *

(d) On request of a party in interest and after notice and hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay —

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest. . . .

* * *

(h) An individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and in appropriate circumstances, may recover punitive damages.

11 U.S.C. § 549 Postpetition Transactions (1988 ed.)

(a) Except as provided in subsection (b) or (c) of this section, the trustee may avoid a transaction of property of the estate —

(1) that occurs after the commencement of the case; and

(2)(A) that is authorized only under section 303(f) or 542(c) of this title; or

(B) that is not authorized under this title or by the court.

Supreme Court, U.S.
FILED
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No. 97-990

In the Supreme Court of the United States

OCTOBER TERM, 1997

FLOYD E. RILEY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether an assessment of liability against petitioner under Section 6672 of the Internal Revenue Code, 26 U.S.C. 6672, that was made after the automatic stay in his bankruptcy case expired is invalid because an administrative notice proposing the assessment was issued during the period of the automatic stay.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	5
Conclusion	8

TABLE OF AUTHORITIES

Cases:

Anderson v. *United States*, 561 F.2d 162 (8th Cir. 1977)	5
Brotherhood of Locomotive Firemen & Enginemen v. *Bangor &Aroostook R.R.*, 389 U.S. 327 (1967)	8
Cleveland Trust Co. v. *United States*, 421 F.2d 475 (6th Cir.), cert. denied, 400 U.S. 819 (1970)	6
Estate of Jones v. *Commissioner*, 795 F.2d 566 (6th Cir. 1986)	6
Luhring v. *Glotzbach*, 304 F.2d 560 (4th Cir. 1962)	6
Olsen v. *United States*, 952 F.2d 236 (8th Cir. 1991)	5
Rosenberg v. *Commissioner*, 450 F.2d 529 (10th Cir. 1071)	6
Ruth v. *United States*, 823 F.2d 1091 (7th Cir. 1987)	5
Slodov v. *United States*, 436 U.S. 238 (1978)	5
United States v. *McCombs*, 30 F.3d 310 (2d Cir. 1994)	5

Statutes:

Act of July 30, 1996, Pub. L. No. 104-168, 110 Stat. 1452:	
§ 901, 110 Stat. 1465-1466	3
§ 901(b), 110 Stat. 1466	4
Bankruptcy Code, 11 U.S.C. 101 *et seq.*:	
11 U.S.C. 106(a)(1)	6
11 U.S.C. 106(a)(3)	6

Statutes—Continued: Page

11 U.S.C. 362 7
11 U.S.C. 362(a)(6) 2, 5
11 U.S.C. 362(b) 2
11 U.S.C. 362(b)(9)(D) 2
11 U.S.C. 362(c) 3
11 U.S.C. 362(h) 6
Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106:
§ 116, 108 Stat. 4119 2
§ 702(a), 108 Stat. 4150 2
Internal Revenue Code (26 U.S.C.):
§ 6672 ..... 2, 3, 5
§ 6672(b) 3
§ 7501 5

Miscellaneous:

Rev. Proc. 84-78, 1984-2 C.B. 754 ..... 4, 6

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A7-A11) is reported at 118 F.3d 1220. The opinion of the district court (Pet. App. A1-A5) is reported at 192 B.R. 727.

JURISDICTION

The judgment of the court of appeals was entered on July 7, 1997. The petition for rehearing was denied on September 16, 1997. The petition for certiorari was filed on December 15, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. During the first three quarters of 1990, Ferco Fabricators, Inc., withheld more than $680,000 in social security and federal income taxes from the wages of its employees. Those taxes were not, however, remitted to the government (Pet. 2; Pet. App. A7-A8). Petitioner was the majority shareholder and chairman of the board of directors of Ferco throughout most of this period (Pet. App. A7).

In September 1991, petitioner sought relief under Chapter 7 of the Bankruptcy Code (Pet. App. A8). The filing of his bankruptcy petition "operate[d] as a stay, applicable to all entities, of * * * any act to collect, assess, or recover a claim against [petitioner] that arose before" the date that the petition was filed. 11 U.S.C. 362(a)(6).[1]

In May 1992, while the automatic stay was in effect, the Internal Revenue Service notified petitioner that it proposed to assess a penalty against him in the amount of $683,675.24 under 26 U.S.C. 6672. That statute imposes a liability against any "person required to collect, truthfully account for, and pay over" withheld taxes who willfully fails to do so. The amount of the proposed assessment was equal to the amount of the 1990 federal withholding taxes that Ferco had failed to pay over to the United States. The letter advised petitioner that he could either

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[1] Section 362(b) of the Bankruptcy Code lists certain exceptions to the automatic stay. After petitioner's bankruptcy case concluded, the Bankruptcy Code was amended prospectively to provide that "the making of an assessment for any tax" is excepted from the automatic stay. Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 116, 108 Stat. 4119. The amendment, which is codified as 11 U.S.C. 362(b)(9)(D), became effective October 22, 1994. § 702(a), 108 Stat. 4150.

agree to the proposed assessment or file an appeal with the IRS within 30 days. Petitioner protested the proposed assessment on the merits and also claimed that it violated the automatic stay (Pet. App. A8).

The automatic stay in bankruptcy expired in June 1992, when the bankruptcy court discharged petitioner of all dischargeable debts (Pet. App. A3). See 11 U.S.C. 362(c). More than a year later, in August 1993, the Internal Revenue Service assessed the amounts due from petitioner under Section 6672. Petitioner paid a divisible portion of the assessment and filed an administrative claim for refund. After the Service denied the claim, petitioner commenced this refund suit (Pet. App. A8).

2. The district court held that the notice of proposed assessment violated the automatic stay and was "void *ab initio*" (Pet. App. A5). The court granted judgment to petitioner on the theory that the notice of proposed assessment "led to" the assessment and that the assessment was therefore invalid (*ibid.*).

3. The court of appeals reversed. The court concluded that the notice of proposed assessment violated the automatic stay, but that the assessment itself—"issued long after the automatic stay expired"—did not (Pet. App. A9). The court noted that, at the time the events of this case transpired, nothing in the Internal Revenue Code required the Service to issue a notice of proposed assessment before issuing the assessment itself.[2] The court concluded that, even if

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[2] Several years after the events in this case, Congress amended the Internal Revenue Code to require that a notice of a proposed assessment be issued prior to assessment under Section 6672. Pub. L. No. 104-168, § 901, 110 Stat. 1465-1466. The amendment, which is codified at 26 U.S.C. 6672(b), applies

the Service ordinarily issued a notice before issuing an assessment under Rev. Proc. 84-78, 1984-2 C.B. 754, that does not make that procedure mandatory: "Revenue Procedures that involve distinctly procedural matters not otherwise controlled by statute * * * are not binding on the agency" (Pet. App. A10). The court held that it would not invalidate an assessment because of a "void" notice "that the agency was under no obligation to issue in the first place" (*ibid.*). The court therefore found it unnecessary to address the "theoretical question" whether the stay violation rendered the assessment "void ab initio, rather than merely 'voidable'" (*id.* at A9 n.1).

The court of appeals also rejected petitioner's alternative argument. Petitioner contended that the assessment should be held invalid as a remedy for the violation of the automatic stay that occurred when the notice of *proposed* assessment was issued. The court concluded that "[w]hatever remedy [petitioner] might be entitled to for the IRS's stay violation is irrelevant to his burden in bringing this refund action" (Pet. App. A10).

The court of appeals therefore reversed the grant of summary judgment in petitioner's favor and remanded the case for further proceedings in the district court (Pet. App. A11).

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only to assessments proposed after June 30, 1996. § 901(b), 110 Stat. 1466.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. Section 6672 of the Internal Revenue Code imposes personal liability on individuals who are responsible for collecting and paying over "trust-fund taxes" on behalf of a corporation but who willfully fail to do so. *Slodov* v. *United States*, 436 U.S. 238, 244-245, 246 n.7 (1978); see 26 U.S.C. 7501. Like other federal tax assessments, an assessment of liability under 26 U.S.C. 6672 is presumptively correct. *United States* v. *McCombs*, 30 F.3d 310, 318 (2d Cir. 1994); *Ruth* v. *United States*, 823 F.2d 1091, 1094 (7th Cir. 1987); *Anderson* v. *United States*, 561 F.2d 162, 165 (8th Cir. 1977). The person against whom Section 6672 liability has been assessed has the burden of proving that he is not responsible or that he did not act willfully in failing to pay over the withheld taxes. *Olsen* v. *United States*, 952 F.2d 236, 239 (8th Cir. 1991).

In his motion for summary judgment, petitioner did not challenge the validity of the Section 6672 assessment on the merits. Instead, he asserted only that the notice of the proposed assessment had been issued in violation of the automatic stay in his bankruptcy case and that the subsequent assessment should therefore be held void. The court of appeals correctly rejected that contention.

Upon the filing of a petition for relief in bankruptcy court, Section 362(a)(6) of the Bankruptcy Code stays "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the [bankruptcy] case." 11 U.S.C. 362(a)(6). The assess-

ment that petitioner challenges in this tax refund suit, however, "was issued long after the automatic stay expired" (Pet. App. A9). The fact that the Service had issued a "notice" of a "proposed" assessment of that tax during the period when the automatic stay was in effect does not make the subsequent assessment itself invalid. As the court of appeals explained, there was no requirement that the Service issue a notice of "proposed" assessment before issuing the assessment in this case (*id.* at A10).[3] Even if the notice of proposed assessment were "void," as petitioner contends (Pet. 4), that would not invalidate the actual assessment of the tax made "long after" the automatic stay expired (Pet. App. A9).

The court of appeals also correctly rejected the contention that petitioner should be absolved from his tax liability as a "remedy" for the issuance of the "proposed" assessment during the period when the automatic stay was in effect (Pet. App. A10). Congress has prescribed a remedy for violations of the automatic stay. Section 362(h) of the Bankruptcy Code authorizes the recovery of compensatory damages, including attorneys' fees, and punitive damages by individuals who are injured by a willful violation of the automatic stay. 11 U.S.C. 362(h); see also 11 U.S.C. 106(a)(1) and (3) (waiving sovereign immunity

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[3] As the court of appeals correctly held, Rev. Proc. 84-78, 1984-2 C.B. 754, which sets forth a notice of proposed assessment scheme, was distinctly procedural and not binding on the IRS. See *Estate of Jones* v. *Commissioner*, 795 F.2d 566, 571-572 (6th Cir. 1986); *Rosenberg* v. *Commissioner*, 450 F.2d 529, 532-533 (10th Cir. 1971); *Cleveland Trust Co.* v. *United States*, 421 F.2d 475, 481-482 (6th Cir.), cert. denied, 400 U.S. 819 (1970); *Luhring* v. *Glotzbach*, 304 F.2d 560, 563-565 (4th Cir. 1962). See note 2, *supra*.

under Section 362, but not for punitive damages). Exoneration of tax liability is not among the prescribed remedies. As the court of appeals correctly noted, whatever the remedy (if any) to which petitioner might be entitled in a proceeding to enforce the automatic stay, it "is irrelevant to [petitioner's] burden in bringing this refund action" (Pet. App. A10). In a refund suit, petitioner must "show that he is not a responsible person or that he did not act willfully in failing to pay Ferco's trust fund taxes" *ibid.* The court of appeals properly remanded the case to the district court for further proceedings on those issues (*id.* at A11).

2. Petitioner errs in contending that the decision in this case implicates a conflict among the courts of appeals as to whether an act that violates the automatic stay is "void" or merely "voidable" (Pet. 4-9). The court of appeals correctly concluded that "this theoretical question [is] beside the point" because the assessment in question was made *after* the stay expired and thus did not violate the automatic stay (Pet. App. A9 n.1): it was neither "void" nor "voidable." That holding does not conflict with any of the decisions that petitioner cites.

3. The court of appeals reversed the award of summary judgment to petitioner and remanded this tax refund case for further proceedings in the district court (Pet. App. A11). Petitioner may now challenge the assessment of liability against him on the merits. If petitioner prevails on remand, and is awarded the refund that he seeks, the issue that he purports to frame in this petition would be made moot. Review of the interlocutory decision of the court of appeals is thus not warranted for this additional reason. See

Brotherhood of Locomotive Firemen & Enginemen v. *Bangor & Aroostook R.R.*, 389 U.S. 327, 328 (1967).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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FEBRUARY 1998